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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: Jeffrey Dorfman
Chief CC:INTL:BR5

SUBJECT:

This Field Service Advice responds to your memorandum dated April 5, 1999. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited as precedent.

LEGEND:

Corp A =
Corp B =
Bank =

Date 1 =
Date 2 =
Date 3 =
Date 4 =
Date 5 =
Date 6 =
Date 7 =

X percent =
Y percent =

Country A =

Amount 1 =
Amount 2 =
Amount 3 =
Amount 4 =
Amount 5 =
Amount 6 =
Amount 7 =
Amount 8 =
Amount 9 =
Amount 10 =
Amount 11 =
Amount 12 =

ISSUES:

1. Whether the issuance and redemption of preferred stock of the taxpayer's subsidiary, which generated a net tax benefit to the taxpayer from foreign tax credits, should be disregarded for federal income tax purposes.

2. Whether the taxpayer's claimed deduction for a foreign exchange loss arising in connection with the preferred stock transaction should be denied.

CONCLUSION:

1. The issuance and immediate redemption of the preferred stock should be disregarded for tax purposes because it is a sham transaction lacking economic substance and a business purpose. The preferred stock transaction was designed to create perfectly offsetting, circular cash flows having no net economic effect. When transaction costs are taken into account, no reasonable possibility of a profit existed, since an economic loss resulted with mathematical certainty. Further, the taxpayer had no business purpose for entering into the transaction other than obtaining U.S. tax benefits. In addition, an argument can be made that the step transaction doctrine may apply to the series of transactions. The transactions were pre-arranged parts of a single transaction intended to generate foreign tax credits under section 902 where economically there was no distribution of earnings and profits. Accordingly, the U.S. tax consequences of the transaction, including a deemed paid foreign tax credit and deductions for interest expense, should be denied.

2. The foreign exchange loss deduction should also be denied since it was a collateral result of the preferred stock transaction. Moreover, it is unclear whether the purported debt (which gave rise to the taxpayer's claimed foreign exchange loss deduction) is actually debt for tax purposes.

FACTS:

Corp A is a U.S. holding company that owns foreign operating subsidiaries. One such wholly owned subsidiary is Corp B, which conducts retail sales of electronic goods in Country A. You have requested our advice concerning a transaction that occurred between Corp A and Corp B.

A. The Preferred Stock Transaction

On Date 1, Corp A acquired Amount 1 shares of preferred stock of Corp B. Corp A paid Amount 2 for these shares. On the same day, Corp B redeemed all of these shares from Corp A for Amount 2. To facilitate the issuance and redemption of the stock, a series of account transfers between Corp A and Corp B bank accounts occurred on June 30 and July 2. Both accounts were located at the same branch of Bank.

By letter dated Date 1, Corp A and Corp B sent instructions to Bank detailing the four transfers to take place on that day. The same individual, who was an officer of both Corp A and Corp B, signed this letter. For reasons unclear to us, Bank did not precisely follow these instructions. Instead it executed only three of the four account transfers on Date 1, as follows:

1. Bank drew an Amount 2 check from Corp B's account and deposited it in Corp A's account. In order to execute this transfer, Bank permitted Corp B's account to be overdrawn by Amount 3. This overdraft was guaranteed by Corp A. The Date 1 letter described the Amount 2 transfer by Corp B to Corp A as "repayment of a loan." (See section B of the facts below.)

2. Bank drew an Amount 2 check from Corp A's account and deposited it in Corp B's account. The Date 1 letter described this check as payment for the issuance of Corp B preferred stock.

3. Bank drew an Amount 2 check from Corp B's account and deposited it in Corp A's account. The letter described this check as payment for the redemption of Corp B preferred stock.

Three days later, by letter dated Date 2, Corp A and Corp B sent instructions to Bank detailing two additional account transfers to take place that day. Again, for reasons unknown to us, Bank executed only one transfer:

1. Bank drew an Amount 2 check from Corp A's account and deposited it in Corp B's account. This transfer was described as a loan from Corp A to Corp B and was used to repay Corp B's overdraft on Date 1.

According to Examination's calculations, the series of transfers between the Corp A and Corp B accounts resulted in net interest expense of Amount 4 for the three day period.

Corp A characterized the Amount 2 payment on the redemption as a dividend. Accordingly, for the tax year ending Date 1, Corp A reported Amount 2 of dividend income from the redemption, as well as a deemed paid foreign tax credit and section 78 gross-up of Amount 5. The dividend and deemed paid taxes were sourced from pre-1987 taxable years of Corp B. (Corp B had a deficit in its post-1986 undistributed earnings pool at the time of the transaction. Corp A also expected Corp B to incur E&P deficits for a number of future years.) The preferred stock transaction resulted in a net U.S. tax benefit of Amount 6 to Corp A (Amount 5 of general limitation foreign tax credits less Amount 12 of pre-credit U.S. tax on the income inclusion of Amount 2 plus Amount 5).

B. <u>The Corp A - Corp B Loan</u>

Corp A had made two advances to Corp B on Dates 3 and 4 that totaled Amount 7. Corp B issued a note to Corp A for Amount 8 denominated in Country A currency (which was equivalent to Amount 7, using the Wall Street Journal closing exchange rate on Dates 3 and 4) bearing interest at X percent. Corp A's tax basis in the note was Amount 7. The note was undated and its terms consisted of a single sentence. Further, the note had no maturity date.

No payments of interest or principal on the loan occurred until the preferred stock transaction. On Date 1 in the first step of the preferred stock transaction described above, Corp B transferred Amount 2 to Corp A's account, which was characterized as partial repayment of the loan. (The repayment was only partial because on Date 1 the Country A currency equivalent of the Amount 2 repayment was less than the principal outstanding on the Amount 8 loan.) Three days later, on Date 2, Corp A reloaned Amount 2 to Corp B. (This advance was the last step of the preferred stock transaction.) Corp B claims to have fully repaid the loan on Date 5.

For financial reporting purposes, the note was treated as a "permanent loan" for which exchange gain or loss would not be reported until Corp A disposed of its entire investment in Corp B. Nonetheless, on its tax return ending Date 1, Corp A reported an exchange gain relating to the note of Amount 9. Corp A later corrected this computation to an exchange loss of Amount 10.

<u>LAW AND ANALYSIS:</u>

I. <u>The preferred stock transaction must be disregarded for federal income tax purposes because it had no real, practical economic effect and had no business purpose.</u>

The preferred stock transaction created perfectly offsetting cash flows comprised of an Amount 2 payment by Corp A for Corp B preferred stock and an Amount 2 distribution to Corp A for redemption of these exact same shares. Because a potential claim to Amount 5 of foreign tax credits was attached to the distribution on redemption, the tax consequence of these offsetting cash flows was a net tax benefit to Corp A of Amount 6 in excess foreign tax credits, which Corp A could use to offset U.S. tax on unrelated foreign source income. Yet the economic consequence of this transaction (apart from U.S. tax benefits), when transaction costs are taken into account, was a predetermined loss of Amount 4 of interest expense. In other words, except for interest expense, Corp A's economic position on Date 1 was no different at the end of the day (after redemption of the Corp B stock) than in the morning (prior to issuance of the Corp B stock).

It is well established that a transaction devoid of economic substance must be disregarded for federal income tax purposes, even where its form indisputably satisfies the literal requirements of the relevant statutory language. See, e.g., Frank Lyon Co. v. United States, 435 U.S. 561, 573 (1978); ACM Partnership v. Commissioner, 157 F.3d 231, 246-47 (3d Cir. 1998), aff'ing in pertinent part T.C. Memo. 1997-115, 73 T.C.M. 2189 (1997); Agro Science Co. v. Commissioner, 934 F.2d 573, 576 (5th Cir. 1991); Rice's Toyota World, Inc. v. Commissioner, 752 F.2d 89, 91 (4th Cir. 1985). Whether a transaction has economic substance is a factual determination and the burden of proof rests with the taxpayer. ACM Partnership, 73 T.C.M. at 2217.

In determining whether a transaction has economic substance, the transaction must be viewed as a whole, and each step is relevant. ACM Partnership, 157 F.3d at 247. Thus, in a prearranged transaction such as the one at hand, all elements of the transaction must be taken into account in performing an economic substance analysis. The analysis in this case necessarily includes the effects and consequences of Corp A's Amount 2 payment for the issuance of Corp B stock and Corp A's receipt of Amount 2 for the stock's redemption, to which Amount 5 of foreign tax credits was attached. Combined, these elements provided the taxpayer with more than $5 million of tax benefits in the form of excess foreign tax credits.

Generally, the inquiry into the economic substance of a transaction looks to the objective economic substance of the transaction and the subjective business purpose behind the transaction. United Parcel Service of America, Inc. v. Commissioner, T.C. Memo. 1999-268 (August 9, 1999). These two aspects of an economic substance inquiry do not constitute a rigid two-step test, but rather represent related factors, both of which inform the analysis. ACM Partnership, 157 F.3d at 247; Sochin v. Commissioner, 843 F.2d 351, 354 (9th Cir. 1988). Because the transaction at issue fails to satisfy either factor, it is an economic sham that should be disregarded for federal income tax purposes.

A. <u>The transaction fails to satisfy the objective aspects of the economic sham analysis.</u>

The phrasing of the objective test has varied among the different courts. For example, the Tax Court in <u>ACM Partnership</u> articulated the objective test as requiring that there be "a reasonable expectation that the non-tax benefits would be at least commensurate with the transaction costs." 73 T.C.M. at 2217. On appeal, the Third Circuit in <u>ACM Partnership</u> repeatedly searched for "any practical economic effects" of a transaction other than the creation of income tax benefits by examining the taxpayer's financial condition before and after the transaction. 157 F.3d at 248-252. Under the Fourth Circuit's expression of the test in <u>Rice's Toyota World</u>, a transaction has no economic substance where "no reasonable possibility of a profit exists." 752 F.2d at 91. <u>See also</u> <u>Friendship Dairies v. Commissioner</u>, 90 T.C. 1054, 1062 (1988). <u>Cf.</u> <u>Killingsworth v. Commissioner</u>, 864 F.2d 1214, 1218 (5th Cir. 1989) (objective analysis involved examination of "profit making potential").

While the specific articulation of the objective test has differed among the courts, the fundamental principle is that a transaction must have real and practical economic effects other than the creation of income tax benefits in order to satisfy the objective aspects of the sham analysis. <u>See</u> <u>Sochin v. Commissioner</u>, 843 F.2d 351, 354 (9th Cir. 1988), <u>cert. denied</u>, 488 U.S. 824 (1988) (objective and subjective factors are considered in determining "whether the transaction had any practical economic effects" other than generating tax benefits); <u>Rose v. Commissioner</u>, 868 F.2d 851, 853 (6th Cir. 1989); <u>Chapman v. Commissioner</u>, T.C. Memo. 1997-147, 73 T.C.M. 2405, 2414 (1997). It is clear that the preferred stock transaction had no real and practical economic effects other than the creation of income tax benefits. Corp A had no reasonable possibility of economic profit, <u>i.e.</u>, no reasonable possibility of income exceeding its costs (Amount 4 of interest expense). Corp A had no possibility of a positive economic return because the transaction was designed to, and in fact did, create perfectly offsetting cash flows, excluding transaction costs. Corp A transferred Amount 2 to Corp B for the issuance of Corp B stock, which was offset by the Amount 2 transferred from Corp B back to Corp A upon redemption of the same shares of Corp B stock. Since the cash flows were designed to net to zero, the transaction costs could never be recovered and an economic loss on the transaction was a mathematical certainty.

Every detail of the transaction was prearranged to and did in fact produce, with virtually no economic consequences, no change in the economic position of the parties. Two letters signed by an officer of both Corp A and Corp B instructed Bank to execute a series of transfers between the Corp A and Corp B bank accounts. The amount of consideration with respect to the issuance and redemption of the stock was predetermined by Corp A and Corp B to ensure that the distribution on redemption perfectly offset the payment arising from the issuance of the stock.

Although Bank did not exactly follow the instructions (and consequently permitted an overdraft in Corp B's account), the end result was nevertheless the same as if Bank had followed the written instructions: the transitory movement of cash between the two accounts netted out to zero within three days, leaving both Corp A's and Corp B's net economic positions at the conclusion of the transaction unchanged (except for transaction costs). Lack of significant change between the parties' positions before and after the transaction is an indicia that the transaction lacks economic substance. Lynch v. Commissioner, 267 F.2d 867, 871-72 (2d Cir. 1959).

Factoring in transaction costs, Corp A could expect only an economic loss before U.S. tax benefits. The absence of risk (upside and downside) is an indication that the transaction is an economic sham. Yosha v. Commissioner, 861 F.2d 494, 500 (7th Cir. 1988) (riskless transactions are mere tax artifices); Heltzer v. Commissioner, T.C. Memo. 1991-404, 62 T.C.M. 518, 529 (1991); Hirai v. Commissioner, T.C. Memo. 1984-495, 48 T.C.M. 1134, 1144 (1984) (denying interest deductions with respect to transactions that had "predetermined ... locked-in" losses).

When viewed as a whole, the presence of a circular cash flow in this transaction reveals its character as an economic sham. See Knetsch v. United States, 364 U.S. 361 (1960); Karme v. Commissioner, 73 T.C. 1163, 1186-87 (1980), aff'd, 673 F.2d 1062 (9th Cir. 1982) (circular money transfers creating illusion of payments indicates lack of economic substance); United States v. Clardy, 612 F.2d 1139 (9th Cir. 1980) (disregarding circular check-swapping payments). The transaction involved the issuance and redemption of stock on the same day for the same amount of consideration, and a series of offsetting transfers between two bank accounts. At the end of the day, the transaction had no practical economic effects on Corp A's or Corp B's economic positions other than the creation of income tax benefits for Corp A. The series of account transfers was nothing more than a superficial, circular payment structure set up as a front for the taxpayer's generation of foreign tax credits. Circular transfers which ultimately do not affect the parties' business positions are strong evidence that the underlying transaction lacks economic substance. Merryman v. Commissioner, 873 F.2d 879, 882 (5th Cir. 1989)("money flowed back and forth but the economic positions of the parties were not altered"); United States v. Crooks, 804 F.2d 1441 (9th Cir. 1986) ("check cyclones" of simultaneous, same-bank transfers of checks left taxpayer in same position as before); Lynch v. Commissioner, 267 F.2d 867, 871-72 (2d Cir. 1959); Medieval Attractions, N.V. v. Commissioner, 72 T.C.M. 924 (1996) (circular movements of cash within single day that are represented only by bookkeeping entries or back-to-back loans and that fail to alter parties' economic positions are a sham).

The funds for the series of transactions at issue were initially derived from a short term, Amount 2 bank loan (the overdraft of Corp B's checking account) which was guaranteed by Corp A. Corp A indicated that Bank was willing to make the loan because of this guarantee, not the inherent creditworthiness of Corp B. This Amount 2 was then transferred to Corp A ostensibly as a repayment of a loan. Corp A then transferred the Amount 2 to Corp B ostensibly for payment of the preferred stock. Corp B ostensibly redeemed the stock in exchange for Amount 2 thus transferring the money back to Corp A. Three days later, Corp A ostensibly loaned Amount 2 to Corp B, which used the funds to repay the bank loan. When this circular flow of funds is collapsed, the net result is that Corp A borrowed Amount 2 on the strength of its own credit for a three day period.

Tax-determined timing and trading patterns are also indicia that a transaction lacks economic substance. Sheldon v. Commissioner, 94 T.C. 738, 766, 769 (1990); Glass v. Commissioner, 87 T.C. 1087, 1174 (1986); Johnson v. Commissioner, T.C. Memo. 1992-369, 63 T.C.M. 3197, 3198-99. Here, Corp A was aware that Corp B had a deficit in its post-1986 undistributed earnings pool at the time of the transaction, and Corp A anticipated E&P deficits for Corp B for a number of future years. In light of these circumstances, the timing of the preferred stock transaction arguably hinged on tax considerations: if Corp A failed to pay any dividends out of pre-1987 E&P years on a timely basis, expected E&P deficits in future years would be carried back on a LIFO basis to eliminate pre-1987 earnings. Because dividends cannot be sourced out of a pre-1987 year whose earnings are absorbed by a deficit carryback, foreign taxes associated with those years could never be deemed paid by Corp A and the foreign tax credit benefit could have been lost. See Treas. Reg. § 1.902-2(a)(1).

The preferred stock transaction fails to satisfy the subjective aspects of the economic sham analysis because the taxpayer has not demonstrated a non-tax business purpose for entering into the transaction.

Like the objective test, various articulations of the subjective test have been set forth by the courts. See, e.g., ACM Partnership, 157 F.3d at 253 (whether the transaction was intended to serve any "useful non-tax purpose"); Rice's Toyota World, 752 F.2d at 91 (whether "the taxpayer was motivated by no business purpose other than obtaining tax benefits in entering in the transaction"); Friendship Dairies, 90 T.C. at 1062 (same). See also Yosha, 861 F.2d at 501 ("Judges can't peer into people's minds or 'weigh' motives.... Rather, the usual approach is to focus the analysis on whether any non-tax goals or functions were or plausibly could have been served by the action."). The common thread of these expressions, however, is whether the transaction has a business purpose other than obtaining tax benefits.

When questioned about its business purpose for the transaction, Corp A responded that Corp B "issued and redeemed the preferred stock in order to preserve cash flow in connection with its [Amount 2] distribution" to Corp A upon redemption of the Corp B stock. Corp A claimed that it saved Amount 11 in cash by structuring the distribution as a redemption of preferred shares. In other words, by choosing this particular form, Corp A avoided a Y percent withholding tax imposed by Country A on gross dividends.[1]

Corp A's argument that foreign tax savings are a valid business purpose for this integrated series of transactions is a red herring. Corp A engaged in this transaction in order to generate a section 902 credit from a circular flow of funds. Since a section 902 credit is triggered by a dividend, one consequence is a potential Country A withholding tax imposed on that dividend. To argue that the business purpose of the transaction is the avoidance of the withholding tax is disingenuous. The potential Country A withholding tax is a direct consequence of the circular flow of funds engaged in to generate foreign tax credits to which Corp A would not otherwise have been entitled. Since the withholding tax would be a direct consequence of an economic sham, avoidance of this consequence cannot serve as a business purpose for engaging in the sham in the first place. Moreover, any such withholding tax would, subject to limitation, be creditable against Corp A's U.S. tax on its foreign source income. Therefore, Corp A's professed business purpose is not consistent with the requirement that a transaction have a non-tax business purpose. See, e.g., ACM Partnership, 157 F.3d at 253 (whether the transaction was intended to serve any "useful non-tax purpose"); Yosha, 861 F.2d at 501 ("whether any non-tax goals or functions were or plausibly could have been served by the action"); Rice's Toyota World, Inc., 752 F.2d at 91 (whether "the taxpayer was motivated by no business purpose other than obtaining tax benefits in entering in the transaction"); Friendship Dairies, 90 T.C. at 1062 (same).

B. Conclusion

The series of transactions at issue gave rise to a circular flow of funds that left Corp A and Corp B in the same economic position as they were in before the transactions took place (absent transaction costs). Corp A has not presented, nor can we deduce, any business purpose for Corp A's involvement in this circular flow of funds. Depending on the earnings of Corp B and subject to limitation under section 904, Corp A will be entitled to a section 902 credit when Corp B pays a dividend to Corp A. Corp A cannot accelerate section 902 credits through a series of transactions that do not amount to a distribution of the earnings of Corp B.

II Application of the Step Transaction Doctrine

[1] The U.S.-Country A income tax treaty, which entered into force on Date 6, imposed a maximum withholding rate on dividends of Y percent. Subsequently, a third protocol was entered into force on Date 7, which reduced the withholding rate.

"The step-transaction doctrine is a corollary of the general tax principle that the incidence of taxation depends upon the substance of a transaction rather than its form." Security Indus. Ins. Co. v. United States, 702 F.2d 1234, 1244 (5th Cir. 1983) (citations omitted). The doctrine provides that transitory phases of a transaction should be ignored when they add nothing of substance to the completed transaction. See Helvering v. Alabama Asphaltic Limestone Co., 315 U.S. 179, 184-85 (1942); see also Minnesota Tea Co. v. Helvering, 302 U.S. 609, 613 (1938) ("A given result at the end of a straight path is not made a different result because reached by following a devious path."). The essence of the doctrine is that in determining tax consequences an integrated transaction should not be broken into separate steps or, conversely, the separate steps should be taken together. See King Enters., Inc. v. United States, 418 F.2d 511, 516 (Ct. Cl. 1969).

In applying the step-transaction doctrine the courts have developed three different tests, with no one being universally applied. See Security Indus., 702 F.2d at 1244; King Enters., 418 F.2d at 516.
The "binding commitment" test, first articulated by the Supreme Court in Commissioner v. Gordon, 391 U.S. 83, 96 (1968), states that a series of actions by a taxpayer will only be treated as a single, integrated transaction if at the time the taxpayer took the first step he was under a binding commitment to take the later steps. See Security Indus., 702 F.2d at 1244.

The less restrictive "end result test" links actions together if they are component parts of a single transaction intended from the outset to be executed for the purpose of reaching the ultimate result. King Enters., 418 F.2d at 516; Penrod v. Commissioner, 88 T.C. 1415 (1987).

The "interdependence test" inquires whether the steps were so interdependent that the legal relations created by one transaction would have been fruitless without a completion of the series. Am. Bantam Car Co. v. Commissioner, 11 T.C. 397, 405 (1948), aff'd, 177 F.2d 512 (3d Cir. 1949). The emphasis under this test is on the relationship between the steps, rather than on the end result. See McDonald's Restaurants of Illinois, Inc. v. Commissioner, 688 F.2d 520, 524 (7th Cir. 1982). Therefore, it is especially proper to disregard the tax effects of individual steps where "it is unlikely that any one step would have been undertaken except in contemplation of the other integrating acts." Kuper v. Commissioner, 533 F.2d 152, 156 (5th Cir. 1976).

As previously stated, the funds for the series of transactions at issue were initially derived from a short term, Amount 2 bank loan (the overdraft of Corp B's checking account) that was guaranteed by Corp A. Corp A indicated that Bank was willing to make the loan because of this guarantee, not the inherent creditworthiness of Corp B. This Amount 2 was then transferred to Corp A ostensibly as a repayment of a loan. Corp A then transferred the Amount 2 to Corp B ostensibly for payment of the preferred stock. On the same day, Corp B ostensibly redeemed the stock in exchange for Amount 2 thus transferring the money back to Corp A. Three days later, Corp A ostensibly loaned Amount 2 to Corp B which used the funds to repay the bank loan. Although more factual development may be needed to support collapsing the transaction under the "end result test" or "interdependence test," we believe that the facts developed to date indicate that application of these tests may be appropriate. In particular, the letters of Date 1 and Date 2, appear to indicate that the series of transactions at issue were component parts of a single transaction intended from the outset to deliver section 902 foreign tax credits without a real distribution of Corp B's earnings. The letters were signed by an officer of both corporations, which committed the corporations to engage in the series of transactions. Moreover, the letters and other facts developed appear to indicate that one transaction would have been fruitless without completion of the series of transactions. These facts implicate all of the three tests.

Finally, when this circular flow of funds is collapsed, the net economic result is that Corp A borrowed Amount 2 on the strength of its creditworthiness for a three day period.

III <u>The taxpayer's claimed deduction for a foreign exchange loss should also be denied since it was a collateral result of the preferred stock transaction. Moreover, it is questionable whether the purported debt is debt for tax purposes.</u>

In determining whether a transaction has economic substance, the transaction must be viewed as a whole, and each step is relevant. <u>ACM Partnership</u>, 157 F.3d at 247. Thus, in a prearranged transaction such as the one at hand, all elements of the transaction must be taken into account in performing an economic substance analysis. Analysis of the preferred stock transaction necessarily includes the effects and consequences of Corp B's purported Amount 2 loan repayment.

Corp A has claimed that it is entitled to a foreign exchange loss deduction incurred in connection with Corp B's purported loan repayment. However, the sole purpose of this transfer was to initiate the transaction's circular cash flow. The loan repayment appears to have no independent economic significance and must be viewed as an element in the overall preferred stock transaction. Accordingly, since the preferred stock transaction should be disregarded an economic sham, so too should the purported loan repayment.

Moreover, it is unclear whether the purported debt at issue is actually debt for tax purposes. The debt is evidenced by an undated note consisting of a single sentence in which Corp B promised to pay Corp A Amount 8 at an X percent interest rate. The note contains no maturity date, and no payments of interest or principal were ever made on the note prior to the transactions at issue. The note was treated for financial reporting purposes as a "permanent loan." Treating the note as debt for tax purposes and equity for financial accounting purposes is a factor that indicates that the note may not be debt. Notice 94-47, 1994-1 C.B. 357. Moreover, failure to make payments under the note and the note's lack of a maturity date also raise questions regarding the treatment of the note as debt for tax purposes.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS:

[redacted]

[redacted]

If you have any further questions, please call (202) 622-3870.

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